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An Overview of Foreign Direct Investment in Mexico

Brandon W. Freeman*

Mexico's economic policy throughout most of the twentieth century has been founded on the principle of self-sufficiency.¹ This perceived need for self-determination resulted in a tightly regulated, isolationist economy.² Mexico's aversion to foreign economic control and political influence can be traced back to the administration of Porfirio Diaz (1876-1911).³ By the end of President Diaz's administration, productive enterprise in Mexico was dominated by foreign capital, and over half the country's wealth was foreign owned.⁴ The large foreign presence in Mexico's economy generated strong anti-foreign sentiment and eventually resulted in the Mexican Revolution of 1910.⁵

The principles behind the Mexican Revolution of 1910 included sovereignty and independence from foreign, economic, and political control.⁶ These principles were embodied in the Mexican Constitution of 1917.⁷ The Mexican Constitution of 1917 is the foundation for the isolationist economic policy and many of the laws that have discouraged and, in some areas, prevented foreign direct investment in Mexico for more than seventy years.⁸ Specific policies that have discouraged foreign direct investment in Mexico include: (1) the prohibition of foreigners from owning land within a restricted zone;⁹ (2) restraints on the creation, modification, liquidation, and transfer of Mexican stock;¹⁰ (3) the prohibition of

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2. Id.
4. Id.
5. Sandrino, supra note 3, at 281.
6. Id. at 283.
8. WHITING, supra note 4, at 55-79.
9. See CONSTITUTION, supra note 7, art. 27.
majority ownership\(^1\) and majority control\(^1\) by foreigners in certain industries; and (4) discriminatory taxation, the awarding of government contracts on a discriminatory basis, and the selective use of permits and licenses.\(^13\) Other factors that have discouraged foreign investment include: (1) the expropriation of foreign owned companies;\(^14\) (2) political insurrection;\(^15\) and (3) currency inconvertibility.\(^16\)

In the last few years, Mexico's economic policy has undergone a dramatic reformation from isolationism to a more open, free market economy.\(^17\) In 1993 the Mexican Congress adopted a new Foreign Investment Law (FIL) that encourages foreign participation in the Mexican economy.\(^18\) In 1994 Mexico entered into the North American Free Trade Agreement (NAFTA) with Canada and the United States.\(^19\) "Chapter 11 of NAFTA (Investment Chapter...) establishes a liberalized investment regime that expands the protection of foreign investors and investments..."\(^20\) In conjunction with the NAFTA, Mexico signed the U.S./Mexico tax treaty which minimizes the burden of double taxation.\(^21\)

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4. In 1938 Mexico expropriated all foreign owned oil companies. HARRY K. WRIGHT, FOREIGN ENTERPRISE IN MEXICO 70 (1971). This oil industry was one of the largest blocks of foreign capital in the country. Id.
5. "Losses from damage" to or the destruction or disappearance of tangible assets caused by politically motivated acts of war or civil disturbance in the host country. Daniel, A New World for Political Risk Investment Insurance, RISK MANAGEMENT Oct. 1994, at 30, 32.
6. "[I]nvestors inability to convert local currency returns (profits, principal, interest, royalties, capital and other remittances) into foreign exchange for transfer outside the host country." Wagner, supra note 15, at 32.
7. See Goldman, supra note 1, at 101.
10. Sandrino, supra note 3, at 262.
Through the adoption of legislation and international treaties, Mexico established an economic policy that encourages and protects foreign direct investment. This comment has three principal parts. The first section gives a brief overview of the important implications of Mexico's FIL and the NAFTA regarding foreign direct investment. The second section gives an overview of the various business enterprises available to foreign investors and the pros and cons of operating under each. The third section discusses two NAFTA side agreements regarding the enforcement of Mexico's labor and environmental laws with respect to their impact on the foreign investor.

I. 1993 Foreign Investment Law.

On December 28, 1993 Mexico adopted a new federal statute entitled the 1993 Foreign Investment Law (FIL). The purpose of the FIL "[i]s to formulate the rules to channel foreign investment into the Nation and to ensure that said investment contributes to the national development." The FIL covers all foreign direct investment in Mexico. A foreign investor is defined as anyone, corporate or individual, other than a Mexican. The FIL opens new areas of investment to foreigners including certain sectors of the oil service industry and the automobile industry. In addition, certain investors are allowed to own property outright, which allows foreign investors who have formed Mexican corporations the freedom to choose and to negotiate their own locations. Furthermore, foreign investors are no longer required to have Mexican partners, but are allowed to control the business alone. The FIL also establishes less ambiguous and less time consuming registration procedures for foreign investors. In effect, the FIL brings Mexico's common law into symmetry with requirements established under the NAFTA.

22. See John M. Vernon & Carole A. Azulaye, A Guide to Implementing Mexico's New Foreign Investment Law, 13 FRANCHISE L.J. 105, 128 (1994). See also Eric Griego, The Labor Dimension of the NAFTA: Reflections on the First Year, 12 ARIZ. J. INT'L & COMP. L. 473, (1995) (noting significant investment barriers in the investment climate in Mexico prior to NAFTA, and the NAFTA's elimination of those barriers); Sandrino, supra note 3, at 327 (noting that Chapter 11 of the NAFTA represents a major departure from Mexico's previous position on foreign investment and international economic relations creating a hospitable environment for foreign investment amongst its signatories); Goldman, supra note 1, at 125 (noting that under Mexico's new policy regarding foreign investment, investors can assure themselves of an ever growing market of consumers). But see Mahmood A. Zaidi, Employment, Trade and Foreign Investment Effects of NAFTA, Minn. J. Global Trade 333 (1996) (using empirical data to illustrate how the NAFTA will have a relatively small impact on the U.S. economy).

23. FIL, supra note 18.
24. Id.
25. Id.
26. Id.
27. Vernon & Azulaye, supra note 22, at 105.
28. Id.
29. Id.
30. Id.
A. Participation in Mexican Companies.

The most significant departure from Mexico's traditional treatment of foreign direct investment is rooted in article 4 of the FIL. Article 4 allows foreign investors to control 100 percent of capital stock in a Mexican enterprise, subject to specific limitations. The specific limitations referred to in article 4 are separated into three categories. The first category includes activities reserved exclusively to the Mexican Government. These activities include: (1) petroleum; (2) basic petrochemicals; (3) electricity; (4) nuclear energy; (5) radioactive materials; (6) satellite communications; (7) telegraph services; (8) radiotelegraphy; (9) mail service; (10) railways; (11) issuance of paper money; (12) mintage of currency; (13) control of ports, airports, and heliports; and (14) any other activity specifically mentioned by applicable legal provisions. The second category is activities reserved exclusively for the Mexican People or to Mexican companies with an "Exclusion of Foreigners Clause." These activities include: (1) domestic land transportation of passengers, tourists and cargo, not including messenger and express package services; (2) retail sale of gasoline and the distribution of liquid petroleum gas; (3) radio and television broadcasting services, excluding cable television; (4) credit unions; (5) developmental banking institutions; and (6) rendering of professional and technical services.

Foreign investors cannot participate in the activities in these two categories either directly or through the use of trusts, agreements, social or statutory covenants, pyramid schemes, or any mechanism granting them control or participation. The only exception is through neutral investment, which is discussed later in this comment.

The third category limits foreign participation in certain areas to set percentages. These percentages are divided into five brackets: (1) up to 10 percent; (2) up to 25 percent; (3) up to 30 percent; (4) up to 49 percent; and (5) over 49 percent. The up to 10 percent bracket includes cooperatives. The up to 25 percent bracket includes domestic air trans-
portation, air taxi transport, and specialized air transportation. The up to 30 percent bracket includes controlling companies of financial groups, multiple banking credit institutions, stockmarket houses, and stock market specialists. The up to 49 percent bracket includes insurance institutions, bond institutions, money exchange houses, manufacturing and marketing of explosives, printing and publication of newspapers, cable television, telephone services, fishing, port services of pilotage to ships, and services related to the railroad sector. The final bracket requires approval by the Foreign Investment Commission (FIC) before a foreign investor may invest in over 49 percent in any of the following activities: private education, legal services, securities appraisal institutions, insurance, cellular telephones, construction of pipelines for transporting oil and gas, and drilling of oil and gas wells.

B. REAL PROPERTY.

The Mexican Constitution prohibits foreigners from owning land within 100 kilometers of Mexico's borders and within 50 kilometers of Mexico's coastline. This area is known as the "restricted zone." However, these restrictions have been eased by the FIL. Mexican corporations having foreign shareholders may now acquire and hold real estate in the restricted zone, provided that real estate is used for nonresidential purposes and the purchase is registered with the FIC. In order for a Mexican corporation to own property in the restricted zone for residential purposes or for foreign natural persons or foreign legal entities to own property in the restricted zone, a real estate trust must be created. Creating a real estate trust requires approval from the FIC. Upon approval, the FIC will issue a permit to a Mexican credit institution authorizing the institution to acquire rights,

43. Id.
44. Id.
45. Id.
46. See, supra note 36. The 1973 Foreign Investment Law established the FIC in order to implement the law and to supervise foreign investment. Id.
47. Id. art. 8.
48. CONST. art. 27.
49. Id.
50. FIL, supra note 18, art. 10.
51. Id. art. 11.
52. Id.
as trustee, on property located in the restricted zone.\(^{53}\) Once the trust has been created, the beneficiaries have full rights to the land, including any benefit from a profit-making operation and exploitation.\(^{54}\) The FIL provides that real estate trusts are valid for fifty years, and renewal is automatic and may continue indefinitely subject to FIC approval.\(^{55}\)

C. NEUTRAL INVESTMENT.

The FIL also expands a foreign investor’s opportunity to invest in “neutral investments.”\(^{56}\) Neutral investment consists of that which is realized in Mexican companies that is not taken into account in determining the percentage of foreign investment in the capital stock of Mexican companies.\(^{57}\) Direct neutral investment may take the form of non-voting shares in which the shareholder has the rights to pecuniary interests in the corporation, but only limited corporate rights.\(^{58}\) Neutral investment shares issued to foreign investors must be approved by the National Securities Commission.\(^{59}\)

D. SANCTIONS.

The FIL also provides several articles that permit sanctions for acts performed in contravention of the law.\(^{60}\) The sanctions range from fines to revocation of authorization to conduct business in Mexico.\(^{61}\) The revocation of authority to do business results in the nullification of all business and statutory agreements, and may be imposed on a Mexican national, Mexican company, foreign national, or foreign legal entity.\(^{62}\)

II. North American Free Trade Agreement.

On January 1, 1994 Mexico entered into the NAFTA with the United States and Canada, thereby creating a free trade area in which tariff and other barriers to trade are greatly reduced.\(^{63}\) Chapter 11 of the NAFTA (Investment Chapter) represents a significant shift in Mexico’s economic policy regarding foreign investments, particularly with respect to treatment, protection against dispossession, and compensation for expropriation of foreign owned property.\(^{64}\)

The NAFTA defines an investor as a NAFTA “Party or state enterprise thereof, or a national or an enterprise of such Party, that seeks to make, is making or has made an

\(^{53}\) Goldman, \textit{supra} note 1, at 120.

\(^{54}\) FIL, \textit{supra} note 18, art. 12.

\(^{55}\) \textit{Id.} art. 13.

\(^{56}\) Vernon & Azulaye, \textit{supra} note 22, at 128.

\(^{57}\) FIL, \textit{supra} note 18, art. 18.

\(^{58}\) \textit{Id.} art. 19.

\(^{59}\) \textit{Id.} art. 20.

\(^{60}\) \textit{Id.} arts. 37-9.

\(^{61}\) \textit{Id.} arts. 37, 38.

\(^{62}\) \textit{Id.}

\(^{63}\) NAFTA, \textit{supra} note 19.

\(^{64}\) Sandrino, \textit{supra} note 3, at 307.
investment." The Investment Chapter is applicable not only to the NAFTA states, but also to investors with substantial business activities in the NAFTA states.

A. TREATMENT STANDARDS.

The NAFTA's Investment Chapter begins by providing general equality of treatment for foreign investors. The provision ensures that foreigners and foreign investments in Mexico are treated equally as national investors in like circumstances with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or disposition of investments. The provision also ensures that NAFTA investors and their investments are accorded at least as favorable treatment as any other investors or investments from other non-NAFTA parties. Thus, a foreign investor in Mexico will not be subject to different or more onerous operating conditions simply by virtue of foreign ownership. This Investment Chapter also provides that no party shall require that a minimum level of investment be held by nationals or require an investor, by reason of its nationality, to sell or otherwise dispose of investment in the territory of the party. Furthermore, no party may require an enterprise that is a foreign investment to reserve certain senior management positions to local nationals.

The NAFTA also requires that investments of a NAFTA party be treated "[i]n accordance with international law, including fair and equitable treatment and full protection and security." Thus, foreign investors will be accorded the same security as nationals, and will not be put at a competitive disadvantage in obtaining permits or authorizations necessary to conduct business operations.

B. PERFORMANCE REQUIREMENTS.

Another important provision of the NAFTA's Investment Chapter is the prohibition of performance requirements. Performance requirements have been a major barrier to investment in Mexico. The Investment Chapter provides that no party shall enforce any commitment or undertaking in connection with the establishment, acquisition, expansion, management, conduct, or operation of an investment of an investor of a party or of a non-party if the commitment is:

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65. NAFTA, supra note 19, art. 1139.
66. Id.
67. Id. art. 1102.
68. Id.
69. Id. art. 1103.
70. Sandrino, supra note 3, at 310.
71. NAFTA, supra note 19, art. 1102.
72. Id. art. 1107.
73. Id. art. 1105(1).
74. Sandrino, supra note 3, at 311.
(a) to export a given level or percentage of goods or services;
(b) to achieve a given level of percentage of domestic content;
(c) to purchase, use or accord a preference to goods produced or services provided in its territory, or to purchase goods or services from persons in its territory;
(d) to relate in any way the volume or value of imports to the volume or value of exports or to the amount of foreign exchange inflows associated with such investment;
(e) to restrict sales of goods or services in its territory that such investment produces or provides by relating such sales in any way to the volume or value of its exports or foreign exchange earnings;
(f) to transfer technology, a production process or other proprietary knowledge to a person in its territory, except when the requirement is imposed or the commitment or undertaking is enforced by a court, administrative tribunal or competition authority to remedy an alleged violation of competition laws or to act in a manner not inconsistent with other provisions of this Agreement; or
(g) to act as the exclusive supplier of the goods it produces or services it provides to a specific region or world market.

This article goes on to prohibit a party from conditioning receipt of advantages in connection with an investment of an investor of a party or of a nonparty on compliance with any of the following requirements:
(a) to achieve a given level or percentage of domestic content;
(b) to purchase, use or accord a preference to goods produced in its territory, or to purchase goods from producers in its territory;
(c) to relate in any way the volume or value of imports to the volume or value of exports or to the amount of foreign exchange inflows associated with such investment; or
(d) to restrict sales of goods or services in its territory that such investment produces or provides by relating such sales in any way to the volume or value of its exports or foreign exchange earnings.

The prohibition on performance requirements is not absolute. A party may still condition the receipt of an advantage, in connection with an investment in its territory of a party or of a nonparty, on compliance with the requirement to locate production, provide a service, train or employ workers, construct or expand particular facilities, or carry out research and development in its territory.

76. NAFTA, supra note 19, art. 1106.
77. Id. art. 1106.
78. Id.
C. TRANSFERS RELATING TO INVESTMENTS.

The risk of currency inconvertibility greatly reduces the amount of foreign direct investment in high risk nations.79 Currency inconvertibility is defined as an "[i]nvestor's inability to convert local currency returns (profits, principal, interest, royalties, capital and other remittances) into foreign exchange for transfer outside the host country."80 Industrialized nations emphasize the importance of a foreign investor's ability to make monetary transfers,81 while most Third World states have exchange control laws to regulate the conversion of currency abroad.82 The NAFTA's Investment Chapter provides the guarantees that industrialized states and their investors and firms seek in order to optimize their investment projects.83

The NAFTA provides that certain transfers relating to an investment shall be made "freely and without delay."84 These transfers include: (a) profits, dividends, capital gains, royalty payments, management fees, technical assistance and other fees, returns in kind, and other amounts derived from the investment; (b) proceeds from the sale of all or any part of the investment or from the partial or complete liquidation of an investment; and, (c) payments made under a contract entered into by the investor, or its investment, including payments made pursuant to a loan agreement. These transfers shall be made in a freely usable currency at the market rate of exchange.85 Certain transfers may be prevented through the goodfaith application of laws relating to: (a) bankruptcy, insolvency, or the protection of creditors; (b) issuing, trading, or dealing in securities; (c) criminal or penal offenses; (d) reports of transfer of currency or other monetary instruments; and (e) ensuring the satisfaction of judgments in adjudicatory proceedings.

D. EXPROPRIATION AND COMPENSATION.

One of the major deterrents to foreign direct investment in developing nations is the possibility of expropriation.86 This possibility is a particularly serious impediment to

79. "The inability to convert local currency creates detrimental consequences for investors. For example, inconvertibility reduces the ability of the investor to meet financial commitments such as the payment of dividends or the withdrawal of profits from the country where the investment is located." George Thomas Ellinidis, Foreign Direct Investment in Developing and Newly Liberalized Nations, 4 J. INT'L L. & PRAc. 299, 316 (1995).
80. Wagner, supra note 15, at 32.
81. Most BIT's prohibit any restrictions placed on the ability of a foreign investor to transfer currency generated in their business enterprise out of the host country. Edward A. Fallone, Going International: Fundamentals of International Business Transactions, American Law Institute, American Bar Association Continuing Legal Education, July 8, 1996.
82. Sandrino, supra note 3, at 315.
83. Id.
84. NAFTA, supra note 19, art. 1109.
85. Id.
investment in Mexico. Expropriation is defined as "the taking of an investor's property without compensation or with inadequate compensation." Public international law recognizes a nation's right to nationalize foreign owned property if: (a) there is no discrimination involved; (b) there is a public purpose; and (c) the foreigner or foreign organization is fairly compensated for the investment. The common problem arising in these situations is determining what constitutes "fair compensation." The NAFTA drafters recognized this problem and appropriately defined the law regarding nationalization in the NAFTA states.

The NAFTA provides that no party may directly or indirectly nationalize or expropriate an investment of an investor in its territory or take a measure tantamount to nationalization or expropriation of such an investment, except when the nationalization is: (a) for a public purpose; (b) on a nondiscriminatory basis; (c) in accordance with due process of law and with treatment in accordance with international law, including fair and equitable treatment; and (d) is accompanied by payment of compensation equivalent to the fair market value, paid without delay and fully realizable with interest from the date of expropriation. This provision in the NAFTA's Investment Chapter marks a significant turn in Mexico's policy toward foreign investment and recognition of the international laws and customs that have been in place between developed nations for many years.

87. Mexico has traditionally viewed expropriation as a major vehicle for self-determination. See generally Sandrino, supra note 3. Accordingly, they have opposed the customary international law governing expropriation. Id. Since Mexico's 1938 oil expropriation, the United States has asserted that the Hull Doctrine is customary international law regarding expropriations. Id. The Hull Doctrine requires prompt compensation for expropriated property in convertible foreign exchange, equivalent to the full value thereof. Id. This has been codified in the Hickenlooper Amendments. 22 U.S.C.A. §2370(e)(1)(1990). Mexico has generally asserted that no international rule existed and that issues of compensation are to be determined by Mexico's laws. See Charter of Economic Rights and Duties of States, G.A. Res. 3281, U.N. GAOR, 29th Sess., Supp. No. 31, at 50, U.N. Doc. A/9631 (1975), reprinted in 14 I.L.M. 251 (1975).


90. Id. at 81.

91. NAFTA, supra note 19, art. 1110.

92. Id.

93. In 1938 President Cardenas signed a decree nationalizing the assets of British owned Royal Dutch Shell and U.S. based Standard Oil of New Jersey. See Wright, supra note 14 at 70. The drastic measure by the Mexican Government was based on the oil companies' refusal to obey the Supreme Court of Mexico's order for increased wages in the oil industry. Id. The Mexican Government's bold move in nationalizing foreign owned oil companies resulted in increased flight in foreign capital. Miguel D. Ramirez, Mexico's Economic Crisis: Its Origin and Consequences 81 (1989). The Mexican Constitution of 1917, which is still in effect today, provides that "expropriations can only be made by reason of utility and by means of indemnity." Const., supra note 7, art. 27. Mexico took this one step further during the oil expropriations, excusing fair compensation when expropriations were "inspired by legitimate causes and the aspirations of social justice." Samuel K.B. Asante, International Law and Foreign Investment: A Reappraisal, 37 Int'l & Comp. L.Q. 588, 599 (citing Reply of Mexican Minister of Foreign Affairs dated Aug. 3, 1938, in Vernon & Azulaye, supra note 30).
E. SETTLEMENT OF DISPUTES.

NAFTA's Investment Chapter establishes a mechanism for the settlement of investment disputes between a NAFTA state and an investor of another NAFTA state. The chapter provides that investors may seek resolution of their claims through international arbitration in accordance with the International Center for Settlement of Investment Disputes Convention or the United Nations Commission on International Trade Law Arbitration Rules.

Under the investor-state arbitration mechanism, an investor, on its own behalf or on behalf of the enterprise the investor owns or controls, may submit to arbitration a claim for loss or damage resulting from the breach by the host state of a treaty provision. An investor's right to arbitration is subject to a three year statute of limitations and notice to the host country at least ninety days prior to submitting a claim to arbitration. In addition, claimants must waive their right to seek resolution through any other means, including the courts under the law of any NAFTA party. However, because the tribunal can only award monetary relief, investors do not waive their right to seek injunctive, declaratory, or other extraordinary relief not involving the payment of damages. The issues in dispute are decided in accordance with the NAFTA treaty and the applicable rules of international law.

The NAFTA's extensive investment dispute mechanism represents a significant departure for Mexico with respect to its recognition of international law in international economic relations. Mexico historically distrusted private-state arbitration mechanisms. This distrust is attributed to the Calvo Clause in the Mexican Constitution, which specifically states that submission to international dispute resolution is in no manner an invocation of diplomatic protection by foreign governments. The implementation of the NAFTA and the New Foreign Investment Law clears “all
doubts about the scope of the 'Calvo Clause' in the Constitution..." and marks a new era in Mexico's international relations.10

III. Business Enterprises.

An important part of an overview on direct foreign investment in Mexico involves exploring the various means of doing business in Mexico. Many different organizational forms are recognized by Mexican Law. These forms are regulated by Mexico's federal law, General Law of Mercantile Organizations111 (Ley General de Sociedades Mercantiles [LGSM]), and the Civil Code (Codigo Civil), "both of which trace their origins to commercial and civil laws of Spain."112 The LGSM applies throughout Mexico, and the various state civil codes are almost identical as to the formation of civil entities.113

IV. Corporate Law.

The most common method for domestic and foreign investors to operate in Mexico is through a corporation.114 Two corporate forms exist under Mexico's corporate law - Sociedad anonima115 (S.A.) and the Sociedad anonima de capital variable116 (S.A.C.V).

11. Justine Daly, Has Mexico Crossed the Border On State Responsibility For Economic Injury To Aliens? Foreign Investment and the Calvo Clause in Mexico After the NAFTA, 25 St. Mary's L.J. 1147, 1181 (1994). Daly addresses the contradiction between the Calvo Clause in the Mexican Constitution and the dispute resolution mechanisms in the NAFTA. Id. Daly argues that Mexico's joining of the NAFTA is not indicative of Mexico's abandonment of the Calvo Doctrine. Id. However, she concedes that in regards to foreign investors the point is moot because the NAFTA provides adequate dispute resolution provisions reducing the probability of the United States asserting diplomatic protection. Id.
112. Marrero, supra note 17, at 129; Phanor J. Eder, Company Law in Latin America, 27 Notre Dame L. Rev. 5 (1951) (commenting about the development of companies under Spanish Law), has observed, in contrast to the rule laid down by Coke and Blackstone and which is still followed in our [common] law, they did not derive their corporate personality from the sovereign, but only their special monopolistic privileges. Id. The corporate or legal personality came from men associating themselves, under the Mexican law, into a “company.” Id. All “companies,” whether formed as a general partnership or as a limited partnership (compania en comandita), had a legal personality adhered automatically to this new form of company, the stock company or anonima, as it was soon to be called. Id. at 15.
113. Edor, supra note 112, at 129.
115. LGSM, supra note 111, art. 87.
116. Id. art. 87.
The S.A. closely resembles the U.S. corporation and is the most formal business organization in Mexico.\textsuperscript{117} The S.A.C.V. differs from the S.A. in that it can decrease its capital within the limits set in the bylaws, by a mere stockholder's resolution without the need to fulfill certain formalities applicable to the S.A.\textsuperscript{118} Shareholders of either an S.A. or an S.A.C.V. are only liable for the amount of capital subscribed.\textsuperscript{119}

A. INCORPORATION.

Companies incorporating in Mexico must follow the corporate name with the initials S.A.\textsuperscript{120} The investors must seek authorization from the Ministry of Foreign Affairs prior to establishment.\textsuperscript{121} Authorization by the Foreign Ministry is reproduced in a notarized deed, which represents the combined articles of incorporation and the bylaws.\textsuperscript{122} An S.A. must consist of at least two shareholders, with no limit on the maximum number, and a minimum capital contribution of 50,000 NP (new pesos), of which at least 20 percent must be paid in immediately.\textsuperscript{123}

B. MANAGEMENT.

Shareholders of a Mexican corporation "are the supreme authority of the corporation."\textsuperscript{124} Shareholders elect either a sole administrator or a board of directors (mandatarios) to manage the affairs of the corporation. Directors are usually elected for one year or until replaced.\textsuperscript{125} If one or more of the directors resides outside of Mexico, it is usually customary to appoint alternate directors in order to facilitate a quorum.\textsuperscript{126} However, no geographical restrictions exist on where a board of directors may choose to convene.\textsuperscript{127} The articles of incorporation normally authorize the board to name a general manager to operate the business of the corporation and should specify any powers that the board may not delegate.\textsuperscript{128} Shareholders have the power to remove directors from the board at

\textsuperscript{117} Marrero, supra note 17, at 130.

\textsuperscript{118} Thomas M. Shoesmith, Investing and Manufacturing: Part I: Basic Business Structuring and The Maquiladora Option, 1 No.1 MEX. TRADE & L. REP. 13 (1991). Changing the amount of capital in an S.A. requires amending the articles of incorporation and approval of the Ministry of Foreign Affairs and, in some cases, the Foreign Investment Commission. Id. Capital reductions also require publication three times in the Official Gazette to provide protection for creditors. PRICE WATERHOUSE, DOING BUSINESS IN MEXICO "INFORMATION GUIDE" (1995).


\textsuperscript{120} LGSM, supra note 111, art. 88.

\textsuperscript{121} PRICE WATERHOUSE, supra note 118, at 84.

\textsuperscript{122} Id.

\textsuperscript{123} WILIAM E. MOOZ JR., AN INTRODUCTION TO DOING BUSINESS IN MEXICO 57 (1995). If contributions are paid in kind, the initial capital must be paid in full. Id. If contributions are paid in cash, a minimum of 20 percent must be paid up front. Id.

\textsuperscript{124} Marrero, supra note 17, at 131.

\textsuperscript{125} PRICE WATERHOUSE, supra note 118, at 87.

\textsuperscript{126} Id.

\textsuperscript{128} Id.
any time. However, directors elected by minority shareholders may only be removed if
the entire board is removed.

In addition to electing directors, shareholders of a Mexican corporation typically
appoint auditors (comisarios) who are responsible for supervising the board of direc-
tors. Auditors are generally lawyers and accountants and serve the function of corpo-
rate council and financial auditor.

C. SHAREHOLDER PROTECTION.

Mexican law protects minority shareholder interests by providing that a shareholder
owning at least 10 percent of the corporate capital of an exchange listed corporation is
entitled to elect at least one director to the board. If the corporation chooses to elect
three or more directors to the board, a minority shareholder owning at least 25 per-
cent of the corporate capital is entitled to select at least one director. Similarly, if the corporation
chooses to appoint three or more auditors, a minority shareholder owning at least 25 per-
cent of the corporate capital is entitled to select at least one.

General shareholder agreements in connection with the management of the corpora-
tion are not recognized under Mexican corporate law. In addition, when important
management issues are decided, extraordinary meetings must be held. Quorum and
super-majority voting requirements are often used in extraordinary shareholder meetings
to protect minority shareholders.

Shareholders are also entitled to enjoin the implementation of a shareholders’ resolu-
tion that is contrary to law or the bylaws of the corporation. Shareholders may also
seek damages for injury to the corporation through a derivative action against the direc-
tors who violate their duties to the corporation. Shareholders filing suit for injunction
or a derivative claim for damages must represent at least one-third of the corporate
capital.

129. LGSM, supra note 111, art. 144.
130. Id.
131. Id. art. 167.
133. LGSM, supra note 111, art. 144.
134. Id.
135. Id. art. 171.
136. Fallone, supra note 132, at 345, See Gomez-Palacio, supra note 119, at 27.
137. PRICE WATERHOUSE, supra note 118, at 87. Extraordinary shareholder meetings must be held to
approve any modification of the articles and bylaws, mergers, or issue of debentures. Id.
138. Fallone, supra note 132, at 345, See Panel Discussion: A Hypothetical Problem on Securities Law, 3
U.S.-MEX. L.J. 93, 102 104 (1995). The articles of corporations with substantial minority share-
holders often provide resolution in key specified areas, such as amendments to the charter, incur-
ring substantial indebted, appointment of higher level employees and their salaries, and may be
approved only by, for example, 60% of the total shares outstanding. PRICE WATERHOUSE, supra
note 118, at 87.
139. LGSM, supra note 111, arts. 201, 202.
140. Id. art. 163.
141. Id. arts. 163, 201, 202.
C. TRANSFER OF SHARES.

Typically, a corporate shareholder may transfer his shares without obtaining the approval of the remaining shareholders. However, the articles of incorporation may condition the transfer of shares upon board approval. The board may deny the transfer of shares to a specific person and in turn designate a different buyer at the market price. Mexican law allows a corporation to purchase their own shares only in limited circumstances.

D. INCREASES AND DECREASES IN CAPITAL.

Before a corporation may reduce the minimum authorized capital stock, the shareholders are required to amend the articles of incorporation at an extraordinary shareholder meeting. In addition, the corporation is required to obtain approval from the Ministry of Foreign Affairs and, in some cases, the Foreign Investment Commission. Corporations are also required to publish capital reductions three times in the Official Gazette in order to provide notice to the corporations’ creditors.

If the corporation reduces the amount of capital, shareholders have the right to redeem some of their shares in proportion to the amount of shares held by each. Likewise, if the corporation decides to issue new shares of stock, shareholders have the right to purchase the new shares in order to maintain their interest in the corporation.

E. SOCIEDAD ANONIMA DE CAPITAL VARIABLE.

Foreign investors may also incorporate as an S.A.C.V. This form is identical to the S.A. except the corporation is not required to fulfill the formalities applicable to the S.A. when the corporation increases or decreases its capital. Requiring minimum formalities for the issue of additional variable capital is important because Mexican corporations are prohibited from owning treasury shares. The procedures for capital increases and decreases of the variable portion of the capital stock should be provided in the company’s articles of incorporation. Typically, the articles provide that increases or decreases in capital may be accomplished by a resolution of the board of directors of an ordinary shareholders’ meeting.

142. Id. art. 130.
143. Id.
144. Fallone, supra note 132, at 345; See Ignacio Gomez-Palacio, supra note 119, at 27. In the United States, corporations are granted statutory power to purchase and to sell shares of its own stock. Del. Code Ann. tit. 8, § 160 (1994). However, the repurchase of outstanding stock with corporate funds may be grounds for a derivative claim by a shareholder if the purchase was improperly centered upon perpetuation of control. Cheff v. Mathes, 199 A.2d 548 (1964).
145. Price Waterhouse, supra note 118, at 86.
146. Id.
147. Id.
148. Id.
149. Id.
150. Marrero, supra note 17, at 131.
151. Price Waterhouse, supra note 118, at 89.
152. Id. at 89.
153. Id. at 89.
V. Limited Liability Companies.

The Sociedad de Responsabilidad Limitada (S.R.L.) is similar to the limited liability company used in many states within the United States.\textsuperscript{154} The Mexican limited liability company has characteristics of a corporation and some characteristics of a partnership.\textsuperscript{155} The form provides limited liability, like a corporation, but the bylaws of the company can be drafted in such a way as to give it most of the characteristics of a partnership.\textsuperscript{156}

Organization of a Mexican limited liability company requires the same prior authorization and registration as the Mexican corporation.\textsuperscript{157} An S.R.L. is limited to fifty members and is subject to a minimum capital contribution of 3000 NP.\textsuperscript{158} These contributions are manifested by “partes sociales,” which are negotiable instruments subject to special provisions.\textsuperscript{159}

The S.R.L. is rarely used as a vehicle for foreign investment.\textsuperscript{160} The membership restrictions render the S.R.L. unsuitable for large businesses.\textsuperscript{161}

VI. Partnerships.

Foreign investors may also form a general partnership (Sociedad en Nombre Colectivo) or a limited partnership (Sociedad en Comandita).\textsuperscript{162} In a general partnership, all partners are jointly liable to creditors of the company.\textsuperscript{163} In the limited partnership, the “socios comanditores” have joint and unlimited liability, and are responsible for all decision making pertaining to the enterprise.\textsuperscript{164} The “financiers,” on the other hand, are only liable for the amount of their capital contribution and may not participate in the management of the business.\textsuperscript{165} The general partnership and the limited partnership are rarely used by foreign investors because of the unlimited liability.\textsuperscript{166}

VII. Joint Venture Contract.

The joint venture contract (asociacion en participacion) is another method of conducting business in Mexico.\textsuperscript{167} In a joint venture contract, a person grants a working

\textsuperscript{154} Marrero, \textit{supra} note 17, at 130.
\textsuperscript{155} Id. at 129-130.
\textsuperscript{156} PRICE WATERHOUSE, \textit{supra} note 118, at 90.
\textsuperscript{157} Id.
\textsuperscript{158} Marrero, \textit{supra} note 110, at 130.
\textsuperscript{159} Id. at 130.
\textsuperscript{160} Shoesmith, \textit{supra} note 118.
\textsuperscript{161} Marrero, \textit{supra} note 17, at 130.
\textsuperscript{162} Id. at 129.
\textsuperscript{163} Id. at 129.
\textsuperscript{164} Id. at 129.
\textsuperscript{165} Id. at 129.
\textsuperscript{166} PRICE WATERHOUSE, \textit{supra} note 118, at 91.
\textsuperscript{167} Id. at 91.
interest in his or her business to others, who provide property or services.\textsuperscript{168} The joint venture contract does not create a separate legal entity like the formation of a Mexican corporation or partnership.\textsuperscript{169} The business is operated by an active managing joint venturer (asociante), who is the only one with any liability to third parties.\textsuperscript{170} There are no registration requirements for entering a joint venture contract and there are no requirements as to minimum capital.\textsuperscript{171}

The joint venture contract provides some particular advantages to foreign investors. The form allows the investor to satisfy ownership requirements present in the host country's laws and allows for better access to, and interactions with, local labor unions, financial institutions, and the government.\textsuperscript{172} Further, the use of a domestic partner yields distribution channels, marketing practices, and cultural and language niceties.\textsuperscript{173} However, the joint venture may limit the partners' ability to modify their commitments to the venture and result in a loss of general flexibility.\textsuperscript{174}

\textbf{VIII. Branch Office.}

Foreign investors may also choose to conduct business in Mexico by establishing a branch office (scursal de sociedad extranjera) after complying with certain formalities and obtaining approval of the Mexican government, including authorization by the Foreign Investment Commission.\textsuperscript{175} A branch office is not treated as a separate legal entity.\textsuperscript{175} Thus, the parent's capital resources may be exposed to any liabilities that accrue in the foreign branch.\textsuperscript{177} For this reason, branches are not a popular vehicle for establishing operations in Mexico.\textsuperscript{178}

\textsuperscript{168} In a joint venture each party may contribute a predetermined amount of capital or the parties may contribute labor, expertise, knowledge, land, and resources, or some permutation of these. \textbf{JOHN P. KARALIS, INTERNATIONAL JOINT VENTURES 7} (1992). Nonmonetary contributions are often assigned a monetary value in order to determine the amount of each parties' contributions. \textit{Id.}

\textsuperscript{169} \textbf{PRICE WATERHOUSE, supra note 118, at 91.}
\textsuperscript{170} \textit{Id.} at 91.
\textsuperscript{171} \textit{Id.} at 91.
\textsuperscript{172} Ellinidis, \textit{supra} note 79, at 305.
\textsuperscript{173} \textit{Id.} at 305.
\textsuperscript{175} \textbf{PRICE WATERHOUSE, supra note 118, at 92.}
\textsuperscript{176} \textit{Id.} at 126.
\textsuperscript{177} \textit{Id.}
\textsuperscript{178} \textit{Id.}
IX. The Maquiladora Program.

The Maquiladora Program was introduced in 1965 as part of the Mexican Border Industrialization Program.\(^{179}\) The Maquiladora Program allows foreign investors to establish 100 percent foreign-owned and managed companies in Mexico.\(^{180}\) The foreign-owned company (maquiladora)\(^{181}\) may import, in-bond and duty free, all the machinery, equipment, and tools to assemble or manufacture any product or component.\(^{182}\) The final products of the maquiladora industry are generally exported for sale outside of Mexico.\(^{183}\)

The maquiladora industry plays a substantial role in the Mexican economy. Maquiladora plants comprise 18 percent of Mexico's manufacturing jobs.\(^{184}\) The total number of workers employed in maquiladoras was over 742,000 by the end of 1995.\(^{185}\) Maquiladoras are the second largest generator of revenue in Mexico's current account, and represent 34 percent of the total value of Mexican exports.\(^{186}\) From these figures, it is apparent that a substantial portion of foreign direct investment in Mexico is represented in the maquiladora industry.\(^{187}\) At year end 1995, U.S. $1.1 billion of total foreign direct investment in Mexico was attributed to maquiladoras.\(^{188}\)

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179. M. Angeles Villarreal, *Maquiladoras: Mexico's Maquiladora Industry*, 2 No. 4 MEX. TRADE & L. REP. 17, 18 (1992). Maquiladoras actually originated in the early 1960's when U.S. companies and Mexican landowners entered into private contracts for the construction of industrial parks. Id. Fearing high unemployment, the Mexican Government encouraged agreements. Id. When the Maquiladora Program was formally established, plant sites were restricted to border zones. Shoesmith, supra note 118, at 14. These restrictions were later modified, allowing the establishment of foreign-owned maquiladoras throughout the interior of Mexico, except in zones of high industrial concentration. Id.


181. The term maquiladora is derived from the Spanish word maquilar. Shoesmith, supra note 118, at 14. A maquilar is an arrangement when a miller retains a portion of the flour he makes in return for providing milling services. Id. Similarly, all facilities involved in the Maquiladora Program involve the processing of foreign inputs. Id. In Mexico, the word "maquilador" has come to mean performing the task for another. Id.

182. Marrero, supra note 17, at 133.


185. Id.

186. Id.

187. The prosperity of the maquiladora industry can be partially attributed to Mexico's low wage rate. Marrero, supra note 17, at 134. When it is possible to separate the labor intensive phase of production from the capital and knowledge intensive phases, "it is beneficial -- in terms of profitability and competitiveness -- to process, assemble, test and package goods in countries with abundant lower cost labor." Id. Wages in Mexico escalated from the all-time low of 54 cents per hour in 1985 to an average of $2 per hour in 1995. *Peso Devaluation Attracts Foreign Plants*, MEX. BUS. MONTHLY, May 1, 1995 available in 1995 WL 8119198. However, the 1995 devaluation of the peso reduced the hourly wage to below $1 per hour. Id.

A. FAVORABLE TARIFF TREATMENT AND RESTRICTIONS ON DOMESTIC SALES.

Traditionally, foreign-owned companies operating as a maquiladora were permitted to import, duty-free, all the machinery, equipment, tools needed for manufacturing, and any raw materials or components, as long as those items were eventually exported out of Mexico for resale. However, the Mexican Government has liberalized the regulations of the maquiladora industry in several stages. The limit on the maquiladora's domestic sales is now governed by the NAFTA. Under the NAFTA, the authorized domestic share of total sales is being raised by 5 percent each year until 2001, when sales are subject to no limitation.

In addition to favorable tarriff treatment in Mexico, final products exported to the United States are given favorable treatment under items 9802.00 and 9802.00.80 of the Harmonized Tarriff Schedule of the United States (HTSUS). The HTSUS provides that tarriffs are levied only upon materials not of U.S. origin and the value added to the original U.S. component by processing in Mexico. Traditionally, U.S. owned maquiladoras have imported 95 percent of materials used in production from the United States.

B. TRANSFORMATION BY NAFTA.

Under the NAFTA, the concept of duty-free importation of raw materials into Mexican maquiladoras will eventually cease. Maquiladoras will then have to pay duties for the foreign raw materials and components instead of holding them on consignment. However, for U.S. companies using maquiladoras as cost centers, the transformation will be one of form and not substance. Goods from the NAFTA partners will be free of duty if they meet the rules of preference, as will the NAFTA goods for all other importers. The NAFTA phases out the duty-free imports for maquiladoras and applies the same duties as imports destined for all other establishments in order to prevent circumvention of the NAFTA parties' external duties.

Asian-owned maquiladoras producing electronic and electrical products will be the principal companies affected by this transformation, because they import most of their raw materials from Asia. U.S. owned maquiladoras however, should continue to pros-
The maquiladora was established primarily with the United States in mind, both as the supplier and as the export market. In fact, three-quarters of the raw material imported by the maquiladora industry is from the United States.

The primary attraction of using maquiladoras as cost centers is Mexico's abundant supply of cheap labor and its proximity to the United States. The differential between U.S. and Mexican wages is expected to persist in the foreseeable future. U.S. companies operating maquiladoras will only benefit from the effects of the NAFTA, as restrictions on domestic sales products will be eliminated. Furthermore, new opportunities will arise for U.S. producers to step in and replace some of the maquiladors' Far Eastern and other third-country suppliers who might lose their competitive advantage because of the new duties. Finally, there will be an incentive for existing maquiladora operations to shift from third-country sourcing to North American sourcing in order to benefit from the NAFTA preferences.

C. ORGANIZATIONAL ASPECTS OF A MAQUILADORA.

Three alternative forms of operations may be considered when establishing a maquiladora: subcontracting, shelter operations, and subsidiaries.

1. The Subcontracting Alternative.

The subcontracting alternative is the least capital intensive method of utilizing the benefits of the maquiladora industry. Under the subcontracting method, a foreign manufacturer must arrange for raw materials or components to be shipped to the maquiladora for assembly or processing. The maquiladora manufactures the materials for the foreign manufacturer on a per unit basis. The subcontracting alternative is the easiest method of operation because of its quick start-up time and ease of termination. However, the efficiency of this method may be lost if the maquiladora subcontractor lacks experience in manufacturing the particular product. In this case, the shelter operation or subsidiary method are perhaps more attractive alternatives.

201. Id.
202. Id.
203. Id.
204. Id.
205. Id.
206. Id.
207. Id.
208. Id.
209. Marrero, supra note 17, at 135.
210. Id.
211. Id.
212. Id.
213. Id. If the maquiladora lacks experience in manufacturing the particular product, the manufacturer may utilize inadequate technology. Id. Furthermore, the foreign manufacturer may face problems such as decreased quality and delivery of the final product. Id. If these risks are realized, the subcontracting alternative may result in a higher cost per unit produced in comparison to the shelter operation and the subsidiary alternative. Id.
2. Shelter Operations.

The shelter operation combines the advantage of ease of start-up and termination associated with the subcontracting alternative with the additional advantage of working with an experienced operator located in Mexico. The shelter arrangement consists of three parties: a foreign-based manufacturer needing the shelter services, a U.S. or Mexican company providing the shelter services, and a Mexican subsidiary of the U.S. company that serves as a vehicle for the assembly or manufacturing operations.

The foreign-based manufacturer needing the shelter services is responsible for supplying the raw materials, certain capital equipment, manufacturing expertise, and management. The company providing the shelter services handles labor, services, customs, and accounting. The Mexican subsidiary is responsible for acquiring the space needed for production, complying with all the applicable Mexican laws and regulations and is the assembler and manufacturer.

Although the shelter operation has the advantage of minimum exposure to Mexican law and provides the ability to work with an experienced operator, the shelter operation may result in less control over technology and product quality and is often more expensive than the subsidiary alternative.

3. The Subsidiary Alternative.

The subsidiary alternative is the third method in which a foreign investor may operate in the maquiladora industry. The foreign company owns 100 percent of the maquiladora and is fully responsible for control of the production process and administration. As a consequence, the foreign manufacturer is responsible for providing extensive managerial support and for complying with all applicable incorporation, real estate, labor, tax, and insurance laws of Mexico.

The subsidiary form is often preferred, especially by large foreign companies, because it allows for total control of every aspect of production. Though this method is naturally more capital intensive, in the long run the per unit cost of production is lower for several reasons. The most obvious reason is that under the subcontracting or shelter alternatives the company in charge of assembly or processing will naturally have an incentive to maximize their profit margin, whereas a subsidiary of the foreign company will operate exclusively as a cost center. In addition, the subsidiary may employ the particu-

214. Marrero, supra note 17, at 136.
215. Id. at 135.
216. Id. at 136.
217. Id.
218. Id.
219. Id.
220. Id.
221. Id.
222. Id.
223. “Virtually all maquiladora companies therefore are organized as wholly-owned subsidiaries....” Shoesmith, supra note 118, at 14-15.
224. Marrero, supra note 17, at 136.
225. Id.
226. Gayou & Gilbert, supra note 114, at 1128.
lar technology and expertise needed to maximize efficiency in the assembly or processing of their particular products. 227

Although the subsidiary alternative is the most cost-effective alternative in the long-run, many small foreign investors are precluded from using this form because of the high start-up costs and long-term commitment involved. 228

X. Mexican Labor Law.

Mexican labor law should be discussed early in counseling all businesses interested in investing or expanding operations into Mexico. 229 This discussion is especially appropriate as arguments are often made that U.S. investors do not establish facilities in Mexico to take advantage of growing consumer markets, but strictly in pursuit of larger profits at the expense of workers' rights. 230 Many U.S. investors perceive Mexico as offering a large, cheap labor force protected by few enforceable labor standards. 231 The question facing today's investors is whether labor costs will remain low and whether labor laws will continue to be sacrificed in order to attract jobs for low-skilled workers.

Mexico has one of the most comprehensive and progressive collections of statutes, regulations, and policies protecting the collective bargaining and other employment rights of Mexican workers. 232 Nevertheless, "[t]he enduring alliance between the government and Mexico's powerful unions has resulted in scant enforcement of Mexican labor law, particularly within facilities owned by foreign investors." 233 However, as a result of the NAFTA side-agreement on labor entitled the North American Agreement on Labor

227. Marrero, supra note 17, at 136.
228. Id. at 135-36.
232. Ann M. Bartow, The Rights of Workers in Mexico, 11 COMP. LAB. L.J. 182, 182 (1990). Mexico was the first country to incorporate basic labor protection in its constitution. Harry K. Wright, FOREIGN ENTERPRISE IN MEXICO 285 (THE UNIV. OF NORTH CAROLINA PRESS, 1971). In fact, Mexico has some of the strongest labor laws in the world, including principles relating to work hours, rest days, vacations, minimum wages and other benefits, occupational safety, discharge of workers, collective bargaining, strikes, and dispute settlement. Id. Most importantly, Mexican labor law clearly favors employees in all dealings with employers, placing many burdensome restrictions on employers. Dubberly, supra note 28, at 42.
233. Louise D. Williams, Trade, Labor, Law and Development: Opportunities and Challenges for Mexican Labor Arising From the North American Free Trade Agreement, 22 BROOK. J. INT'L L. 361, 372 (1996). The Confederacion de Trabajadores de Mexico, Mexico's largest labor organization, has historically been closely tethered to Mexico's powerful El Partido Revolucionario Institucional (PRI). Id. at 375. In light of the historical affiliation between the Mexican Government and Mexico's labor unions, Mexican labor law has provided a setting for continuous dealmaking and mutual gain for the PRI and for labor leaders. Id. at 374.
Cooperation (NAALC),\footnote{The NAALC was signed by the leaders of the three nations in September 1993, North American Agreement on Labor Cooperation, Sept. 14, 1993, U.S.-Can.-Mex., 32 I.L.M. 1499, (1499)[hereinafter NAALC], and became effective on January 1, 1994. Id. at 1514. "The NAALC establishes a tri-national dispute resolution scheme seeking specifically to respond to differences in labor regulation throughout North America." Michael J. McGuinness, Recent Development, The Protection of Labor Rights in North America: A Commentary on the North American Agreement on Labor Cooperation, 30 Stan. J. Int'l L. 579, 582 (1994). The NAALC sets forth several principles protecting the rights of labor, including: (1) the right to organize; (2) the right to bargain collectively; (3) the right to strike; and (4) minimum employment standards. NAALC, supra, note 733 at 1515. Article 27(1) of the NAALC established the Commission for Labor Cooperation to oversee enforcement proceedings against any nation which demonstrates a persistent pattern of failure to enforce its labor laws. Id. at 1509. In articles 15 and 16, the NAALC established the National Administrative Offices (NAO), which are responsible for receiving and investigating public communications or complaints related to labor law issues in the territorial domain of another party. Id. at 1507. Article 29(1) of the NAALC gives the NAO the power to initiate a formal review of any complaints and to impose monetary fines (article 39) and suspension of treaty benefits (article 41). Id. at 1509, 1511-1513.} which was demanded by President Bill Clinton as a condition of supporting the NAFTA, this lack of enforcement may not persist indefinitely.\footnote{Dubberly, supra note 228, at 42. Prior to the passage of the NAFTA, a process of intense discussion and analysis culminated as a result of the fear that closer economic integration with Mexico would result in a shift of U.S. investment to that country, and downward pressure on U.S. wages and benefits. Jorge F. Perez Lopez & Eric Griego, The Labor Dimension of the NAFTA: Reflections on the First Year, 12 Ariz. J. Int'l & Comp. L. 473, 473-74 (1995).} Some argue that the NAALC will result in much more vigorous enforcement of the Mexican labor laws.\footnote{Dubberly, supra note 228, at 42. It is also argued that Mexico's currency crisis has created considerable pressure to increase government revenue through greater enforcement of regulations, including labor regulations. Id. at 41.} However, in light of recent decisions pursuant to the NAALC, it appears the NAALC does not provide an opportunity to address the concerns of Mexico's failure to enforce its labor law, particularly with respect to the rights of employees to organize and to form unions as was anticipated.\footnote{Daniel Friedenzohn, Note, The "Reality" Faced by Mexican Employees Who Lose Their Jobs: A Review of The North American Agreement on Labor Cooperation and Two U.S. National Administrative Office Decisions, 22 Syracuse J. Int'l L. & Com. 103 (1996). In two complaints, pursuant to the NAALC, the issue was whether the Government of Mexico properly complied with and effectively enforced its labor laws guaranteeing the workers' right to associate and to freely organize in the workplace. Id. at 111-14. In both submissions, the dismissed employees decided to accept severances offered by the companies. Id. Thus, the NAO decided it was not in a position to determine whether Mexico enforced its relevant labor laws. Id. at 114.} Whether the NAALC is an effective tool in addressing concerns about lack of enforcement of Mexico's labor laws remains to be seen.\footnote{Id. at 123. "Whether this exchange of information and the ability for interested parties to file complaints with their respective NAOs leads to better enforcement and fairer trade between the two countries remains to be seen." Id. at 126. The NAALC is the first time the United States negotiated an agreement addressing labor issues to supplement an international trade agreement. Id. at 103.} The NAALC was not drafted with the intent of changing Mexico's weak enforcement of labor laws, but as a tool to provide
insight into how the labor laws of a country operate. Nevertheless, active use of the NAALC may only generate better labor protection for workers in all NAFTA countries through the enforcement of labor laws. Thus, foreign investors should be apprised of Mexican labor laws and take such laws into consideration when determining the costs of investing in Mexico.

XI. Mexican Environmental Laws.

Foreign investors considering doing business in Mexico should also be aware of the North American Agreement on Environmental Cooperation, known as the supplemental agreement. This agreement is a result of the fear that economic growth would come at the expense of necessary environmental protections.

The NAFTA ensures that each party to the agreement has the right to promulgate and to enforce its own domestic environmental laws. The supplemental agreement provides that: (a) each party must effectively enforce its environmental laws and regulations; and (b) each party shall ensure that its laws and regulations provide for high levels of environmental protection and shall strive to continue to improve those laws and regulations.

In addition, the supplemental agreement created the Commission for Environmental Cooperation, which has jurisdiction to handle parties' claims when there has been a

239. Id. at 126.
240. Id.
241. Dubberly, supra note 228, at 42.
244. NAFTA, supra note 19, art. 904 provides that "[e]ach party may in accordance with their agreement, adopt, maintain or apply any standards-related measure, including any such measure relating to safety, the protection of human, animal or plant life or health, the environment or consumers, and any measure to ensure its enforcement or implementation." Id.
245. Supplemental agreement, supra note 241, at 1483-84.
246. Supplemental agreement, supra note 241, at 1484.
“persistent pattern of failure by the Party complained against to effectively enforce its environmental law.”

The relevance of the supplemental agreement to foreign investors should be apparent. Mexico’s enforcement of its environmental laws has been notably lethargic, and thus has enticed U.S. companies to relocate there to avoid the more restrictive environmental laws in the United States. If Mexico’s labor laws are more strictly enforced, foreign investors will have to consider the cost of such enforcement when determining whether to relocate to or to start a new company in Mexico. However, whether the supplemental agreement will result in increased environmental regulations is yet to be seen. It is argued that the supplemental agreement will be ineffective in causing Mexico to enforce its envi-

248. Supplemental agreement, supra note 241, at 1490. “[T]he CEC is the powerhouse of the Supplemental Agreement.” Alicia A. Samios, NAFTA’s Supplemental Agreement: In Need of Reform, 9 N.Y. Int’l L. Rev. 49, 65 (1996). “The functions of the CEC are twofold: (1) it provides a forum for request of environmental records; and (2) it resolves disputes concerning non-enforcement of domestic environmental laws.” Id.

249. See Jane J. Duffer, Dump at the Border, PROGRESSIVE, Oct. 1988, at 24, 28. American companies are lured into Mexico because of their ability to bypass environmental regulations. Id. “It’s all too easy for the U.S. companies to turn a blind eye to such incompetence [of waste handling and disposal] when they know how much money they’re saving by disposing of the wastes in Mexico.” Id. Although required by law to return all hazardous materials to the country of origin, American companies have been known to engage in illegal dumping by surreptitiously transporting their waste trucks to Mexico. See Michael L. Connor, comment, Maquiladoras and the Border Environment: Prospects for Moving from Agreements to Solutions, 3 Colo. J. Int’l Envtl. L. & Pol’y 683 (1992). Richard Wolkomir, Hot on the trail of toxic dumpers and other eco-outlaws, Texastyle, SMITHSONIAN 26, 27 May (1994)(reporting on recent incident in which the FBI caught an American company attempting to dump 171 drums of PCB wastes in El Paso); Gene M. Grossman & Alan B. Krueger, Environmental Impacts of Nafta In the Mexico-U.S. Trade Agreement 13, 15 (Peter M. Garber ed. 1994). Elizabeth A. Ellis, Note, Bordering on Disaster: A New Attempt To Control The Transboundary Effects of Maquiladora Pollution, 30 Val. U. L. Rev. 621, 621 (1996)(attributing “forty-two cases of anencephalic babies” in Matamoros to the maquiladora industry).

Nevertheless, foreign investors should be aware of the increasing awareness of environmental concerns, which includes anticipating more stringent enforcement of environmental regulations.

XII. Conclusion.

Mexico’s adoption of the Foreign Investment Law and the North American Free Trade Agreement opened the doors to foreign direct investment. Business opportunities for the foreign investor in Mexico are better than they have been for fifty years. Investors will make better decisions by considering the cultural differences and the history of foreign-investment regulation in Mexico.

Although this comment provides an overview of several factors to be taken into account prior to planning a strategy for entering the Mexican market, investors should consider Mexico’s laws with particular regard to the enterprise sought to be formed. Additionally, obtaining legal counsel who has both experience doing business in Mexico and established contacts with the Mexican legal community is crucial for the foreign investor to navigate through the many complex and unfamiliar laws and customs of Mexico.

251. See Samios, supra note 246, at 76. “Unfortunately the Supplemental Agreement, as it is currently structured, does not serve as an adequate protector of the environment.” Id. “Major shortcomings of the supplementary agreement include its: 1) failure to provide non-citizens access to private remedies; 2) lack of representation of non-governmental interests; 3) limitation on the scope of matters that the panel can address; 4) its vulnerability to political manipulation; and 5) its deviation from traditional arbitration.” Id. See Ellis, supra note 247, at 661-76 (noting that the supplemental agreement as it is currently drafted will be ineffective in its attempts to protect the border from the transboundary effects of maquiladora pollution). Ellis points out that the primary failure is the inability for the environmental standard to be enforced on an individual level by targeting the profit margin of facilities which do not comply with environmental regulations. Id. at 627.

252. See Goldman, supra note 1., See also Sandrino, supra note 3.


254. Id.

255. Id. at 801; Marrero, supra note 17, at 140.